

Online Research @ Cardiff

This is an Open Access document downloaded from ORCA, Cardiff University's institutional repository: <https://orca.cardiff.ac.uk/id/eprint/135301/>

This is the author's version of a work that was submitted to / accepted for publication.

Citation for final published version:

Molla Imeny, Vahid, Norton, Simon D. ORCID: <https://orcid.org/0000-0001-8337-0944>, Salehi, Mahdi and Moradi, Mahdi 2021. Taxonomies of money laundering: an Iranian perspective. Journal of Money Laundering Control 24 (2) , pp. 348-360. 10.1108/JMLC-07-2020-0074 file

Publishers page: <http://dx.doi.org/10.1108/JMLC-07-2020-0074>
<<http://dx.doi.org/10.1108/JMLC-07-2020-0074>>

Please note:

Changes made as a result of publishing processes such as copy-editing, formatting and page numbers may not be reflected in this version. For the definitive version of this publication, please refer to the published source. You are advised to consult the publisher's version if you wish to cite this paper.

This version is being made available in accordance with publisher policies.

See

<http://orca.cf.ac.uk/policies.html> for usage policies. Copyright and moral rights for publications made available in ORCA are retained by the copyright holders.



**Taxonomies of Money Laundering: An Iranian Perspective**

Journal:	<i>Journal of Money Laundering Control</i>
Manuscript ID	JMLC-07-2020-0074
Manuscript Type:	Scholarly Article
Keywords:	Money laundering, Financial Action Task Force, Iran, Golden Triangle, Palermo Convention, Terrorist financing

SCHOLARONE™
Manuscripts

Taxonomies of Money Laundering: An Iranian Perspective

Structured abstract

Purpose – To identify the sources of laundered money in Iran and the destinations to which it is transferred, independently verified by auditors. Based on such data, to develop a simple model of endogenous and exogenous factors facilitating money laundering in developing countries which can inform domestic and international legislative and regulatory responses.

Design/Methodology/Approach– Questionnaires were sent to Iranian certified public accountants who worked for auditing firms in 2019 and who have encountered suspected money laundering during their work with clients.

Findings – The government and public officials are the primary sources of money laundering activity in Iran. The main destinations of laundered funds are investments abroad, gold, foreign currencies, real estate, and purchases of luxury goods. Domestic legislation, whilst bearing similarities with that found in other jurisdictions such as the United Kingdom and the United States, is flawed in several ways, including an inability to determine beneficial ownership of funds and weak enforcement.

Originality/value – Due to international sanctions and the prevailing political situation, it is difficult to obtain data for money laundering and other financial crimes in Iran. The data obtained is of importance to international bodies in understanding the nature of money laundering in Iran, and how to negotiate in the future to address mutual concerns. Given the country’s perceived high association with money laundering, the data obtained is of value in identifying the specific characteristics of the problem.

Category: Research paper.

Keywords: Money laundering. Financial Action Task Force. Iran. Terrorist financing. Golden Triangle. Palermo Convention.

1. Introduction

In advanced economies money laundering is invariably associated with sophisticated techniques intended to avoid the attention of investigators (Mitchell *et al.*, 1998; Simser, 2008; Irwin *et al.*, 2012). ‘Smurfing’, or the use of individuals to transfer high volumes of small cash payments into the financial system, goes against this perceived sophistication but is more associated with small-scale illicit drug transactions. In contrast, in developing countries the crime is associated with people smuggling, drug production and manufacture, and bribery and corruption, perhaps by politicians who take ‘back handers’ on the awarding of government contracts. For example, in Colombia the illegal narcotics industry is the main source of illicit funds (Thoumi, 2002). In Brazil, the major sources of illicit funds are smuggling, corruption, narcotics trafficking, and organised crime (Bijos, 2014). In China, the source of illicit funds is more related to corruption and insider dealing rather than drugs and violent crimes (Naheem, 2017). In India, the main sources of dirty monies are corruption, fraud, currency counterfeiting, organized crimes, human trafficking, and drug trafficking and the main tool for money laundering is *hawala* (Kar, 2011). In Pakistan, money laundering is associated with terrorist financing where drug trafficking, kidnapping and extortion generate illicit funds (Azam and Javaid, 2017). Iran shares several of these factors and has been blacklisted by the Financial Action Task Force (FATF) for its involvement with money laundering which, according to the head of the organisation, puts the international financial system at risk.

Regarding the sources of Iranian laundered funds, first impressions would suggest that this is principally derived from trade in illicit narcotics across the region: it is, after all, one of three countries making up the ‘Golden Triangle’ of the international drugs trade, the other two being Afghanistan and Pakistan (Chalk, 2010; Sabatelle, 2011). The country’s political leadership would deny any association with terrorism-related money laundering but the European Union, the United States, and the FATF, take a different view. The difference arises from a tautology: Iran does not accept the international community’s view that Lebanon’s Hizbullah is a terrorist organisation, nor Iraq’s Hashado Shabi, nor Yemen’s Ansarollah, and that as such, any payments to these groups, through charities or government financial support, cannot, by definition, constitute terrorist financing. This diametrically opposite interpretation of what constitutes a terrorist organisation is the main reason for the country’s refusal to accede to the Palermo Convention and the Terrorist

1
2
3
4
5
6
7
8
9
10
11
12
13
14
15
16
17
18
19
20
21
22
23
24
25
26
27
28
29
30
31
32
33
34
35
36
37
38
39
40
41
42
43
44
45
46
47
48
49
50
51
52
53
54
55
56
57
58
59
60

Financing Convention of 1999, both of which underpin the FATF’s efforts to reduce terrorist-related money laundering (Matsuoka, 2018). These two sources of laundered funds- drugs and terrorism- come to mind in the context of Iran but as explained, there are several others which are common to developing countries generally. The research questions addressed in this paper are as follows. First, what are the actual as opposed to preconceived sources of money laundering in Iran? Are these the same as in other developing countries, or are there nuanced differences? Second, what are the destinations of Iranian laundered money? If both the sources and destinations are domestic, then these should be addressed and counteracted through national legislation. However, if there is an international dimension, then this raises questions about the architecture of conventions and legislation which exist beyond Iranian jurisdiction. To criticise the country for failings which happen outside its borders is to risk criticising the speck in its eye – its domestic shortcomings which enable money laundering to take place - whilst overlooking the beam in the eye of the international financial community. The next section provides a literature review of money laundering in developing countries. Section 3 develops a simple theoretical model of exogenous and endogenous factors contributing to money laundering in developing countries. Section 4 provides empirical data regarding sources and destinations of laundered funds in Iran. Section 5 applies the model to the findings and discusses the implications for domestic reform and international enforcement. Section 6 concludes.

2. Literature review

In a speech in Chatham House, London, in January 2010, introducing the United Kingdom government’s new anti-bribery strategy, the Lord Chancellor stated that the World Bank estimated that a trillion dollars a year are paid in bribes. Politicians and public officials in developing and transition economies are estimated to receive between twenty and forty billion dollars in bribes each year despite ostensibly robust anti-corrupt payments legislation found in most advanced economies. For example, the United Kingdom’s Bribery Act 2010, based on the Organisation for Economic Cooperation and Development’s 1997 Anti-Bribery Convention, makes it a strict liability offence for partnerships and companies to fail to prevent bribery, principally through the

making of payments to foreign public officials to obtain a business advantage. The sources of dirty money in developing countries have been investigated by Vaithilingham and Nair (2007). They focused on technology (information and communication technology infrastructure), the quality of human capital, effectiveness of legal frameworks, and corporate governance and ethics within firms. They found that an efficient legal framework combined with good corporate governance lower the pervasiveness of money laundering. In a report produced by the World Bank in 2012 on controlling the flow of illicit funds from developing countries, edited by Peter Reuter, several factors were identified as drivers of money laundering. First, tax evasion resulting from failure to create social consensus and political ambition to build a legitimate and effective state. This political economy aspect of money laundering can be described thus: if there is a lack of consensus on the need to pay taxes to fund political stability and economic growth, combined with a lack of administrative capacity to collect taxes, and if regime leaders and elites are unwilling to tax themselves, then money laundering and an outflow of dirty money will persist (Petanlar *et al.*, 2011). Tax evasion is perceived as dissatisfaction with government, political interference in the economy, and weak governance (Lewis, 1982; Kim 2008).

In Columbia geography has been a significant obstacle to economic integration and an obstacle to effective central state presence throughout the country. The country has a large informal economy; financial services cover only a minority of the population, illegal economic activities are widespread, and violence, sometimes allegedly conducted by government proxies, is frequently used to achieve economic goals. Law enforcement is problematic, undermined by political and societal corruption. Iran has a similar large informal economy but in contrast to Columbia, state control is highly centralised and the government's writ runs throughout the entire country and is not excluded from regions or provinces (Khandan and Nili, 2014). Money laundering is also associated in developing countries with human trafficking: most profits made by petty traffickers are retained in the country in which they are derived, but it is the core businesses of criminal organisations such as prostitution, illegal drugs, counterfeiting, corruption, where the high profits are made. In the World Bank Report of 2012, Maton and Daniel considered 'The kleptocrat's portfolio decisions', showing how politically exposed persons (PEPs) involved in corrupt activities in Kenya, Indonesia, Uganda, and Zambia, including two former heads of state, were able to amass fortunes offshore in tax havens, and were also able to evade civil asset recovery powers. They noted that those charged with offences are invariably more able to hire lawyers able to oppose

1
2
3
4
5
6
7
8
9
10
11
12
13
14
15
16
17
18
19
20
21
22
23
24
25
26
27
28
29
30
31
32
33
34
35
36
37
38
39
40
41
42
43
44
45
46
47
48
49
50
51
52
53
54
55
56
57
58
59
60

prosecutions than the persons pursuing them. The situation is exacerbated by an unwillingness of politicians who subsequently come to power to pursue those who came before them and have looted the country.

Otusanya (2011) linked money laundering to political corruption in developing countries, and the extent to which it significantly damages economic development. Sharman and Chaikin (2009) considered how systems of laws, regulations and institutions developed to counter money laundering provide powerful tools for fighting corruption. They questioned why such tools are not used in developing countries in combatting corruption, given that they can easily and at low cost be deployed in this additional context. They proposed that anti-money laundering (AML) systems can be used to fight corruption because of the focus on the importance of financial intelligence, asset confiscation, and international cooperation. However, such systems as proposed by outside powerful actors, for example the FATF, suffer from a lack of ownership in developing countries, leading to their adoption in a tokenistic fashion to enhance international legitimacy and reputations. Sharman (2008) noted that in 1988 not a single country had a policy against money laundering, but twenty years later over 170 countries had broadly similar AML policies in place. This extensive diffusion was puzzling because it had not been conclusively proven that such policies work. Sharman argued that this process of diffusion was much more power-based than voluntary. The mechanisms driving policy diffusion including direct coercion, mimicry, and competition, were all discursively mediated exercises of power, rather than reflecting rational learning or brute material forces.

Genuine compliance by developing countries with FATF requirements, and with obligations prescribed in Conventions such as Palermo and the Terrorist Financing Convention, has been questioned in the literature (Johnson, 2002). Masciandaro (2005) considered the policy consequences of the pros and cons of the blacklisting procedure, finding that lax financial regulations combined with the high cost of compliance can undermine a country's aspiration to meet its FATF obligations. Eggenberger (2018) has questioned the legitimacy of the process of blacklisting, identifying three prerequisites for effectiveness: the stigma of being blacklisted, the nature of sanctions imposed in support, and the blacklist's legitimacy. Mugarura (2013) observed that global anti-money laundering laws are often emasculated by the fact that they are implemented in the realm of international law which manifests itself within independent member states' vested

1
2
3 strategic self-interests. In the event of conflicts, national self-interests will prevail. But money
4 laundering is an opportunistic crime because it generates both synergies and externalities and the
5 response of an individual state often depends on how it is affected by it. In not acceding to the
6 required international conventions as stipulated by the FATF, Iran has experienced significant
7 reputational damage, being one of only two countries on the blacklist (Rahmdel, 2018). Force has
8 also been applied to encourage compliance (as well as in response to the international community's
9 concern about nuclear proliferation in the region), in the form of sanctions which have had a
10 profound economic impact. The country has also been placed at a competitive disadvantage vis a
11 vis its neighbours in failing to attract foreign direct investment. However, the legitimacy of the
12 blacklisting process as explained by Eggenberger (2018) has been questioned by the Iranian
13 government because of differing interpretations as to what constitutes a terrorist organisation,
14 averred to earlier. Paradoxically, when the country does eventually comply with the Conventions,
15 this may be less tokenistic than has been the case with other developing countries as criticised by
16 Sharman and Chaikin (2009). The next section develops a model of factors facilitating money
17 laundering in developing countries which will be applied later in the context of Iran.
18
19
20
21
22
23
24
25
26
27
28
29
30
31

32 **3. A simple endogenous and exogenous modelling for money laundering in developing** 33 **countries** 34 35 36 37 38

39 It can be seen from the literature that causes of money laundering are both endogenous and
40 exogenous. Regarding the former, factors would include the lack of will and the resources to
41 enforce domestic legislation, absence of accountability of politicians, and the ineffectiveness of
42 anti-corruption laws and procedures (Markovska and Adams, 2015; Sharman and Chaikin, 2009).
43 Sharman (2008) indicates that corruption and money laundering often go hand in hand; corrupt
44 politicians who have looted the state need to find effective ways to launder their illegal gains.
45 Other endogenous factors include the extent of the informal economy; the greater this is, the greater
46 the opportunity for money laundering (Ponsaers *et al.*, 2008). In August 2016 the Iranian English
47 Economic Daily, the *Financial Tribune*, noted that Iran's informal economy (the part of the
48 economy which does not pay taxes and is not monitored by state agencies, for example regarding
49 labour rights or safety in the workplace) employs a third of the workforce, and generates a fifth of
50
51
52
53
54
55
56
57
58
59
60

economic output. The Minister of Cooperatives, Labour and Social Affairs, Ali Rabiei, stated in a conference in May 2016 that of 22.5 million people presently employed in the country, sixteen million are formally employed, leaving 6.5 million in the informal sector. According to the former head of the National Tax Administration, Ali Askari, and reported in the *Financial Tribune* article, tax revenues are below 7% of GDP, in contrast to 25-30% in most developed countries. According to the Ministry of Economic Affairs and Finance, in the fiscal year 2015-16, the informal economy accounted for 36.5% of GDP compared with 7% in 1974-75. Accountants who fail to report clients' undeclared earnings to the appropriate authorities, or assist them in evading taxation, perpetuate and exacerbate the informal economy and in so doing make money laundering more likely (and even socially acceptable). The same is true of financial institutions which receive or pay out to payers or beneficiaries suspected of concealing their identity. The remainder of this section will examine these endogenous and exogenous factors in detail.

3.1. Endogenous factors facilitating money laundering

A significant endogenous factor contributing to money laundering pertains to the political economy of a country and the extent to which elites understand the obligation to pay taxes for economic and social advancement (Hassan and Prichard, 2016). This in turn is a product of social cohesiveness; if a society is atomised and individualistic, or if evasion of taxes is regarded as socially or morally acceptable, then the size of the illegal economy and with it money laundering as a corollary, will increase (Storm, 2013). The size of Iran's informal economy has resulted in an increase in tax evasion and money laundering in recent decades. A connected endogenous factor is the ability of central government to impose its will and to ensure compliance with AML laws across the country, for example in individual provinces. A highly decentralised state with significant levels of regional autonomy such as Columbia has resulted in limited central government fiat and a proliferation of tax evasion, money laundering and an illicit trade in narcotics as a result. In contrast Iran is, governmentally, a highly centralised state which would suggest an ability to enforce AML rules across the country (Higgins, 1984). However, the existence of multiple authorities in Iran has increased the level of corruption (Hen-Tov, 2007) ; bribery, embezzlement, abuse of power, and other forms of corruption in Iranian governmental

1
2
3 agencies is significant. This coincides with findings by Alamdari (2005) who observed that, from
4 a political economy perspective, instead of horizontal layers of classes the power structures in both
5 Shi'ism and clientelism are based on vertical columns of rival and autonomous groups. The
6 traditional Shi'ah institution of *Marja'iyat* (source of emulation which provides religious
7 interpretation on matters of law), has come into conflict with an elected government. A reformist
8 government elected in 1997 failed to deliver on its democratic promises and to end the role of
9 autonomous groups; for Alamdari, disenchanted with state-sponsored reforms, Iranian society
10 seemed to be moving towards pragmatism and utilitarianism, while the political power structure
11 leans towards militarism. Central government is therefore principally concerned with 'holding the
12 ring' between competing groups within the political architecture (Atabaki, 2005), rather than in
13 designing and enforcing effective AML rules from the centre.
14
15
16
17
18
19
20
21
22
23
24

25 **3.2. Exogenous factors facilitating money laundering**

26
27
28

29 Exogenous factors include the effectiveness of enforcement of asset recovery processes in foreign
30 courts. This in turn depends on recognition of Iranian domestic court rulings in foreign courts, and
31 of orders regarding the freezing of bank accounts held in foreign jurisdictions. There are two
32 international conventions covering enforcement of court rulings in the region: the Riyadh Arab
33 Agreement for Judicial Cooperation 1983, and the 1996 Gulf Cooperation Council Convention for
34 the Execution of Judgments, Delegations and Judicial Notifications (the GCC Convention). The
35 former has 18 signatories across the Arab world, while the latter is limited to the six members of
36 the GCC. Both Conventions cover matters including the recognition and enforcement of civil
37 judgements, including the freezing of bank accounts suspected to be linked to looting of the state
38 by politicians or public officials, money laundering and corruption, rogatory assistance by
39 domestic courts in support of foreign proceedings, and the service and recognition of legal
40 documents such as orders freezing assets. Iran is not a signatory to either Convention: this is a
41 significant exogenous weakness in any attempt to pursue the proceeds of money laundered by, for
42 example, bureaucrats or corrupt officials if these have been moved outside the jurisdiction to
43 neighbouring states (Askin and Collins, 1993; Chamberlain, 2002). Other exogenous factors will
44 include the availability of offshore financial centres to Iranian launderers, and their ease of
45
46
47
48
49
50
51
52
53
54
55
56
57
58
59
60

accessibility (Otusanya and Lauwo, 2012). Launderers also need to invest in overseas assets such as high value property, with the collusion of local advisors such as estate agents and lawyers (He, 2006). Foreign banks which assist capital flows to offshore accounts, or provide informal and unlicensed conversion of currencies, or fail to properly record or report the identity of beneficiaries, also assist in the money laundering process (Peterson, 2013). Having developed this simple model of endogenous and exogenous factors facilitating money laundering in developing countries, the next section will provide the results of field research in Iran regarding the balance between the two.

4. Research findings

A questionnaire was e-mailed to Iranian audit firms and then followed up with phone calls in which the objectives of the research were explained. This method of investigation is widely accepted in academic research of this nature (Babbie, 2012). Accounting professionals, particularly auditors, are expected as part of their professional duties to be aware of signs of money laundering and then to report these to the appropriate authorities, principally through the filing of Suspicious Activity Reports (Melnik, 2003; Mitchell *et al.*, 1998;; Norton, 2018). Accordingly auditors have an important role to play in counteracting money laundering (Salrhi et al., 2019; Cox, 2014; Standing and Van Vuuren, 2003). In 2019, 253 audit firms with 1,008 CPAs were operating in Iran (available at <http://en.iacpa.ir/Membership>): these provided the statistical population for this research. We received 148 responses (14.7% of our research sample). The opinions expressed in the questionnaire were well informed on the issue of money laundering: when asked about awareness of domestic laws regarding money laundering and FATF requirements, 17.6% said they had average knowledge of the former, 63.5% good, and 14.7% excellent. For awareness of the latter, the corresponding percentages were 37.9%, 27.7%, and 8.1%.

4.1. Sources of laundered funds

The main sources of dirty funds in Iran as deduced from the questionnaires are presented in Table 1. The principal sources comprise bribery in government, smuggling of goods, undeclared earnings, and the illicit narcotics trade (Farzanegan, 2009). These results are consistent with prior academic research noted earlier. Although respondents also believed that bribery involving company contracts and criminality by the military are also significant sources of dirty funds, their importance is less than the five others. Some respondents also considered human trafficking and sanctions evasion as two other sources of dirty funds in the country, but the activity was statistically insignificant. The results are presented in Table 1.

Table 1
Main statistics of sources of dirty funds in Iran

	N	Mean	Mdn	Std	Sk	Kurtosis	Min	Max
Bribery in government and contracts	148	4.35	5.00	0.92	-1.40	4.36	1.00	5.00
Bribery in companies and contracts	148	3.76	4.00	1.03	-0.49	2.49	1.00	5.00
Drugs money	148	4.06	4.00	1.13	-1.01	2.99	1.00	5.00
Undeclared earnings	148	4.35	5.00	0.86	-1.38	4.56	1.00	5.00
Military	148	3.51	4.00	1.40	-0.41	1.84	1.00	5.00
Smuggling of goods	148	4.43	5.00	0.83	-1.86	7.24	1.00	5.00
Terrorism	148	3.61	4.00	1.27	-0.49	2.16	1.00	5.00
Petty or small crime, for example by taxi drivers, shop keepers	148	2.34	2.00	1.26	0.64	2.39	1.00	5.00

Mdn is the abbreviation of median, Std is the abbreviation of standard deviation, and Sk is the abbreviation for Skewness.

Table 1 comprises mainly endogenous factors relating to the sources of money laundering. For example, receipt of bribes by government officials, undeclared earnings, petty crime, and corrupt payments made for company contracts (so-called 'back handers'). Of these, bribery in government and undeclared earnings are the most significant sources, according to auditors who completed the

questionnaire. However, smuggling of goods was deemed more significant at a mean of 4.43 compared to 4.35 for these other two factors. Terrorism is a significant source and has a mean of 3.61. The military as a source of money laundering has a mean of 3.51, whilst drugs money is at 4.06. The military, by virtue of its presence in other countries, is also able to channel illegal funds beyond the reach of domestic courts (Tangri and Mwenda, 2003). These latter four factors are exogenous in nature: they take place at the interface between Iran’s domestic jurisdiction and the outside world. For example, drugs flow across the ‘Golden Triangle’; money is taken by Iranian parties as intermediaries as the drugs pass through from the producer regions of Afghanistan and Pakistan to the consumer markets of the West (Sen, 1992; Sabatelle, 2011). Similarly terrorist funding flows out from Iran to recipients or proxies in neighbouring states (subject to the observation that, should these payments be made to organisations not recognised as terrorist by the Iranian government, then tautologically these do not represent terrorist flows), constituting a further externality (Rudner, 2010).

4.2. Destinations for laundered funds

Table 2
Main statistics of the destination of laundered monies in Iran

	N	Mean	Mdn	Std	Sk	Kurtosis	Min	Max
Investing in securities	148	2.92	3.00	1.30	0.11	1.94	1.00	5.00
Purchasing shares in companies.	148	3.18	3.00	1.26	-0.06	2.01	1.00	5.00
Purchasing real estate	148	4.25	5.00	0.90	-0.85	2.54	2.00	5.00
Purchasing luxury goods	148	4.13	4.00	1.02	-0.88	2.71	1.00	5.00
Transferring outside national borders	148	4.51	5.00	0.88	-1.86	5.76	1.00	5.00
Payments to family or to friends	148	3.08	3.00	1.21	0.00	2.05	1.00	5.00
Purchasing gold and foreign currencies	148	4.30	5.00	0.82	-0.83	2.63	2.00	5.00

Mdn is the abbreviation of median, Std is the abbreviation of standard deviation, and Sk is the abbreviation of Skewness.

Table 2 identifies the destinations for Iranian laundered funds as ranked by auditors who completed the questionnaire. These comprise both endogenous and exogenous considerations. Regarding the former, there are investments in government and corporate bonds, ranked with a mean of 2.92. There are also payments to family and associates, with a mean of 3.08. Both these factors should be dealt with domestically. For example, the Iranian Stock Exchange imposes rules by which investors in securities must be named and their names appear on share certificates and registers of members. Transfers to family should be within the competence of the tax authorities to deal with, although it is accepted that present practice is unsatisfactory as evidenced by the low tax take achieved. However, exogenous factors are considerably more significant in terms of how they were ranked by respondents. Transfers outside national borders had a mean of 4.51, whilst purchases of gold and foreign currencies had a mean of 4.3. Both activities require the collusion of foreign intermediaries, whether this be passive ('looking the other way' and not filing a SAR), or active (for example, deliberately bidding for high value art at an auction sale on behalf of a known PEP, or buying real estate on his or her behalf).

Transfers of funds out of Iranian jurisdiction require foreign banks to process these (unless the physical cash is loaded into boats or lorries and transported across borders), and for foreign third parties such as lawyers or estate agents to invest the proceeds on behalf of, and to the instruction of, the launderer. This is the integration stage of money laundering: illegal funds become part of the financial system and difficult to trace. Failure of the country to accede to conventions which would enable such funds to be pursued represents a significant exogenous weakness. However, failure of foreign financial intelligence units and prosecutorial authorities to detect or intercept such illegal flows from Iran represents a weakness for which the government cannot be held responsible. For example, in January 2018 the United Kingdom introduced Unexplained Wealth Orders under the Criminal Finances Act 2017 to seize assets unless and until the owner can explain the origin of funding. Failure to utilise such orders and comparable orders in other developed countries, reflects two failures: first, that of the Iranian government to prevent the initial crime (endogenous weakness), and second, that of the UK or other overseas authorities to make use of the appropriate legislative instrument to seize it (an exogenous failure for which the former cannot be held to blame). Most respondents considered Canada, Turkey, the UAE, the USA, the UK,

Panama, Russia, Georgia, China, and tax havens, as the main destinations for laundered money from Iran. Of this list, the US, UK, and Canada have exceptional investigative powers and asset seizure legislation, and yet are identified by auditors as being preferred destinations for dirty money. This suggests that, despite the present sanctions regime, flaws in the system are still enabling launderers to move money out of the country. Hence, before the international community condemns the speck in Iran's eye, which is of course of a considerable size, it should first recognise the beam in its own eye which makes the flows of funds out of the country possible. The next section critiques the extent to which endogenous and exogenous factors are addressed in current Iranian legislation.

5. AML legislative provisions in Iran: a critique

In a Public Statement issued in October 2019 the FATF provided the following explanation of its policy towards Iran:

‘Until Iran implements the measures required to address the deficiencies identified with respect to countering terrorism-financing in the Action Plan, the FATF will remain concerned with the terrorist financing risk emanating from Iran and the threat this poses to the international financial system. The FATF, therefore, calls on its members and urges all jurisdictions to continue to advise their financial institutions to apply enhanced due diligence with respect to business relationships and transactions with natural and legal persons from Iran, consistent with FATF Recommendation 19, including: (1) obtaining information on the reasons for intended transactions; and (2) conducting enhanced monitoring of business relationships, by increasing the number and timing of controls applied, and selecting patterns of transactions that need further examination’.

FATF concerns, and those endogenous and exogenous factors identified in the previous section, should already be capable of addressed by the appropriate domestic authorities using legislative provisions which already exist in Iran. According to Article 49 of the Constitution of the Islamic Republic of Iran:

The government has responsibility for confiscating all wealth accumulated through usury, usurpation, bribery, embezzlement, theft, gambling, misuse of endowments, misuse of government

contracts and transactions, the sale of uncultivated lands and other resources subject to public ownership, the operation of centres of corruption, and other illicit means and sources, and restoring it to its legitimate owner. If no such owner can be identified, it must be entrusted to the public treasury’.

This Article predates provisions in the UK Proceeds of Crime Act 2002 and the US Patriot Act 2001 by a couple of decades (the Constitution was introduced in 1979), and shares both the means and the objectives of these later statutes. Subsequently Article 662 of the Islamic Penal Code was ratified in 1996, criminalising dealing with the proceeds of theft; Note 2 of Article 119 of the Penal Code of the Armed Forces further criminalised obtaining the proceeds of embezzlement. It is apparent from these provisions that Iran already has in place the statutory mechanisms allowing for the seizure of illegally obtained earnings, notwithstanding that they do not specifically refer to money laundering *per se*. The first major legislative attempt by the Iranian authorities to combat money laundering as a distinct crime was in 2002. In the Regulations Concerning Prevention of Money Laundering through Financial Institutions and its 24 articles, money laundering and suspicious transactions were formally defined. The Regulations require banks and other financial institutions to fully implement know your customer protocols, to effectively supervise the activities and operations of their customers, and not to render any type of banking service to ‘prohibited persons’, which would include organisations deemed terrorist by the government (Salehi and Imeny, 2019). However, in the FATF Statement of February 2019, weakness in customer verification was identified as a continuing failing in banks’ AML procedures.

In 2008 the Iranian Parliament ratified a further Anti-Money Laundering Law, refining the definition of money laundering. The Anti-Money Laundering High Council was constituted the body responsible for coordinating agencies involved in AML (the Financial Intelligence Unit, or FIU). However, the FATF identified as continuing failings the lack of independence of the FIU and the lack of protection afforded to whistleblowers. In 2016, Iran focused on countering terrorist financing by ratifying the Combating the Financing of Terrorism Law. This law provided a further refinement of the definition of terrorism. It also extended this definition to include predicate offences such as handling illegal money or opening accounts through which it can be channeled, prescribed applicable penalties, and laid out the reporting obligations of different entities. However, the reality is that these laws continue to fall short in material respects, including

1
2
3
4
5
6
7
8
9
10
11
12
13
14
15
16
17
18
19
20
21
22
23
24
25
26
27
28
29
30
31
32
33
34
35
36
37
38
39
40
41
42
43
44
45
46
47
48
49
50
51
52
53
54
55
56
57
58
59
60

identification of true beneficiary and transferor of funds through wire transfers, and dealings with charities. Existing legislation fails to adequately counteract endogenous factors facilitating money laundering and falls short in terms of effective enforcement. However, in contrast to other developing countries which experience these endogeneities, Iran does have specific and targeted legislation ‘on the books’: what is lacking, amongst other reasons, is the political will to enforce it (Sohrabi *et al.*, 2016). Regarding the exogenous factors identified as sources in Table 1, these are more serious and, possibly, beyond the remit of the Iranian state to oppose. Specifically, the inability to trace laundered moneys into foreign accounts, inhibited by the country’s failure to accede to relevant conventions for civil recovery through foreign courts, will continue to hobble efforts to recover proceeds of criminal activity by public officials, the military, and others who hide their ill-gotten gains in foreign locations (Scher, 2005; Simser, 2010; Smellie, 2005).

6. Conclusion

The main reason for Iran’s inclusion on the FATF blacklist is its failure to accede to the Palermo and Terrorist Financing Conventions. In 2019 the FATF identified deficiencies in the country’s AML regime including not identifying and freezing terrorist assets in line with United Nations resolutions, inadequate customer due diligence, inadequate reporting of suspicious transactions, and lack of information about the originator and beneficiary of wire transfers. This paper has shown that the taxonomy of money laundering in Iran is more nuanced than this general critique by the FATF would suggest. We have proposed that factors facilitating money laundering, both in Iran and in other developing countries, are better analysed and dealt with if seen as being either endogenous or exogenous in nature. With regard to the former, these are factors within the purview of the government; Iran has the domestic legislative instruments to deal with the crime of money laundering but failure to do so may be attributable to a lack of political will, or to save embarrassment of those presently in government or public service, or who have retired from either. Exogenous factors are the responsibility of financial intelligence units in other countries. The view of auditors is that weaknesses in the international financial system are the main facilitators of transfers of funds relating to terrorism, drug dealing, currency purchases, and purchases of high value overseas assets. Iran’s failure to accede to civil recovery conventions mean that such moneys

cannot be traced and recovered through foreign courts. However, other jurisdictions do have mechanisms at their disposal to deal with this, and in so doing to make the flow of dirty money more difficult. These include, for example, Unexplained Wealth Orders in the United Kingdom which enable assets to be seized and held unless and until the owner explains the source from which they were purchased. The taxonomies of money laundering in Iran are complex, comprising weaknesses in the domestic legislative architecture which are exacerbated by endogenous factors- weaknesses in the international domain- over which the country has no control. In negotiating with Iran and encouraging the country to comply with the Palermo and Terrorist Financing Conventions it is important to bear in mind that, whilst domestic factors which bring about money laundering can be addressed using existing legislation, there is also a need for the international community to prevent the flows of illicit funds to jurisdictions where there is already appropriate legislation in place but which, according to our findings in the questionnaire administered to auditors, is similarly inadequately enforced.

References

Alamdari, K. (2005), “The power structure of the Islamic Republic of Iran: transition from populism to clientelism, and militarization of the government”, *Third World Quarterly*, 26 (8), 1285-1301.

Askin, S. and Collins, C. (1993), "External collusion with kleptocracy: can Zaire recapture its stolen wealth?", *Review of African Political Economy*, Vol. 20 No. 57, 72-85.

Atabaki, T. (2005), "Ethnic diversity and territorial integrity of Iran: domestic harmony and regional challenges", *Iranian Studies*, Vol. 38 No. 1, 23-44.

Bijos, L. (2014), "*The Crime of Money Laundering in the Brazilian Legislation*", Paper presented at the 10th Annual Conference, Italian Society of Law and Economics, Università degli Studi di Roma–La Sapienza, Facoltà di Giurisprudenza.

Chalk, P. (2010), "Southeast Asia and the Golden Triangle's heroin trade: threat and response", *Studies in Conflict and Terrorism*, Vol. 23 No. 2, 89-106.

Chamberlain, K. (2002), "Recovering the proceeds of corruption", *Journal of Money Laundering Control*, Vol. 6 No. 2, 157-165.

Cox, D. (2014), *Handbook of Anti-Money Laundering*: John Wiley and Sons, London.

Eggenberger, K. (2018), "When is blacklisting effective? Stigma, sanctions and legitimacy: the reputational and financial costs of being blacklisted", *Review of International Political Economy*, Vol. 25 No. 4, 483-504.

Farzanegan, M. R. (2009), "Illegal trade in the Iranian economy: Evidence from a structural model", *European Journal of Political Economy*, Vol. 25 No. 4, 489-507.

FATF. (2012-2018). *International Standards on Combating Money Laundering and the Financing of Terrorism and Proliferation*. Paris, France.

FATF. (2019). *Public Statement - October 2019*. Retrieved from Paris.

Hassan, M. and Prichard, W. (2016), "The political economy of domestic tax reform in Bangladesh: political settlements, informal institutions and the negotiation of reform", *Journal of Development Studies*, Vol. 52 No. 12, 1704-1721.

He, P. (2006), "Lawyers, notaries, accountants and money laundering", *Journal of Money Laundering Control*, Vol. 9 No. 1, 62-70.

Hen-Tov, E. (2007), "Understanding Iran's New Authoritarianism", *The Washington Quarterly*, Vol. 30 No. 1, 163-179.

Higgins, P.J. (1984), "Minority- state relations in contemporary Iran", *Iranian Studies*, Vol. 17 No. 1, 37-71.

Irwin, A.S.M., Choo, R. K., and Liu, L. (2012), "An analysis of money laundering and terrorism financing typologies", *Journal of Money Laundering Control*, Vol. 15 No. 1, 85-111.

Johnson, J., and Lim, D.Y.C. (2002), "Money laundering: has the Financial Action Task Force made a difference?", *Journal of Financial Crime*, Vol. 10 No. 1, 7-22.

Khandan, A. and Nili, M. (2014), "Government interventions and the size of the informal economy. The case of Iran (1971–2007)", *Journal of Economic Policy Reform*, Vol. 17 No. 1, 71-90.

Kim, S. (2008). "Does Political Intention Affect Tax Evasion?" *Journal of Policy Modeling*, Vol. 30 No. 3, 401–15.

Lewis, A. (1982), *The Psychology of Taxation*, Palgrave Macmillan. Basingstoke, United Kingdom.

Markovska, A. and Adams, N. (2015), "Political corruption and money laundering: lessons from Nigeria", *Journal of Money Laundering Control*, Vol. 18 No. 2, 169-181.

Masciandaro, D. (2005), "False and reluctant friends? National money laundering regulation, international compliance and non-co-operative countries", *European Journal of Law and Economics*, Vol. 20, 17-30.

Mashali, B. (2012), "Analyzing the relationship between perceived grand corruption and petty corruption in developing countries: case study of Iran", *International Review of Administrative Sciences*, Vol. 78 No. 4, 775-787.

Matsuoka, A. (2018), "Ratify and comply: a pathway for Japan to follow the FATF recommendations", *Journal of Money Laundering Control*, Vol. 21 No. 1, 71-88.

Melnik, S. V. (2003), "Accountants' Anti-Money-Laundering Responsibilities", *The CPA Journal*, Vol. 73 No. 12, 50-51.

Mitchell, A., Sikka, P., and Willmott, H. (1998), "Sweeping it under the carpet: The role of accountancy firms in moneylaundering", *Accounting, Organizations and Society*, Vol. 23 No. 5-6, 589-607.

Mugarura, N. (2013), "An appraisal of United Nations and other money laundering and financing of terrorism counter measures", *Journal of Money Laundering Control*, Vol. 16 No. 3, 249-265.

Naheem, M. A. (2017), "Money laundering and illicit flows from China—the real estate problem", *Journal of Money Laundering Control*, Vol. 20 No. 1, 15-26.

Norton, S. D. (2018), "Suspicion of money laundering reporting obligations: Auditor compliance, or sceptical failure to engage?", *Critical Perspectives on Accounting*, Vol. 50, 56-66.

Otusanya, J. (2011), "Corruption as an obstacle to developemnt in developing countries: a review of literature", *Journal of money Laundering Control*, Vo. 14 No. 4, 387-422.

1
2
3 Otusanya, J. and Lauwo, S. (2012)., "The role of offshore financial centres in elite money
4 laundering practices: evidence from Nigeria", *Journal of Money Laundering Control*, Vol. 15 No.
5 3, 336-361.

6
7
8
9 Petanlar, S. K., Gilak, M. T., Samimi, A. J., and Aminkhaki, A. (2011), "An Estimation of Tax
10 Evasion in Iran", *Journal of Economics and Behavioral Studies*, Vol. 3 No. 1, 8-12.

11
12
13
14 Peterson, B. (2013), "Red flags and black markets: trends in financial crime and the global banking
15 response", *Journal of Strategic Security*, Vol. 6 No. 3, 298-308.

16
17
18
19 Ponsaers, P., Shapland, J., and Williams, C.C. (2008), "Does the informal economy link to
20 organised crime?", *International Journal of Social Economics*, Vol. 35 No. 9, 644-650.

21
22
23
24 Rahmdel, M. (2018), "FATF and money laundering in Iran", *Journal of Money Laundering*
25 *Control*, Vol. 21 No. 3, 314-327.

26
27
28
29 Reuter, P. (2012), *Draining development? Controlling flows of illicit funds from developing*
30 *countries*, World Bank, Washington.

31
32
33
34 Rudner, M. (2010). Hizbullah terrorism finance: fund-raising and money laundering. *Studies in*
35 *Conflict and Terrorism*, 33 (8), 700-715.

36
37
38
39 Sabatelle, D. R. (2011), "The scourge of opiates: The illicit narcotics trade in the Islamic Republic
40 of Iran", *Trends in Organized Crime*, Vol. 14 No. 4, 314-331.

41
42
43
44 Salehi, M., and Molla Imeny, V. (2019), "Anti-money laundering developments in Iran: Do Iranian
45 banks have an integrated framework for money laundering deterrence?", *Qualitative Research in*
46 *Financial Markets*, Vol. 11 No. 4, 387-410.

47
48
49
50 Salehi, M., Molla Imeny, V., and Khaleghi Baygi, A. (2019), "The necessity of anti-money
51 laundering standards for Iranian auditors", *Journal of Money Laundering Control*, Vol. 23 No. 1,
52 187-207.

1
2
3 Scher, D. (2005), "Asset recovery", *African Security Review*, Vol. 14 No. 4, 17-26.
4
5

6
7 Sen, S. (1992), "Heroin trafficking in the golden crescent", *The Police Journal*, Vol. 65 No. 3,
8 251-256.
9

10 Sharman, J.C. and Chaikin, D. (2009), "Corruption and anti-money laundering systems: putting a
11 luxury good to work", *Governance*, Vol. 22 No. 1, 27-45.
12
13

14
15 Simser, J. (2008), "Money laundering and asset cloaking techniques", *Journal of Money*
16 *Laundering Control*, Vol. 11 No. 1, 15-24.
17
18

19
20 Simser, J. (2010), "Asset recovery and kleptocracy", *Journal of Financial Crime*, Vol. 17 No. 3,
21 321-332.
22
23

24
25 Smellie, A. (2005), "Prosecutorial challenges in freezing and forfeiting proceeds of transnational
26 crime and the use of international asset sharing to promote international cooperation", *Journal of*
27 *Money Laundering Control*, Vol. 8 No. 2, 104-114.
28
29

30
31 Sohraby, F., Habibitabur, H., and Masoudzade, M. R. (2016), "Money Laundering Crime and Its
32 Situational Prevention in Iranian Law and International Law", *Journal of Politics and Law*, Vol. 9
33 No. 7, 57-63.
34
35

36
37 Standing, A., and Van Vuuren, H. (2003), "The role of auditors: Research into organised crime
38 and money laundering", *Institute for Security Studies Papers*, Vol. 73, 1-16.
39
40

41
42 Storm, A. (2013), "Establishing the link between money laundering and tax evasion", *International*
43 *Business and Economics Research Journal*, Vol. 12 No. 11, 1437-1450.
44
45

46
47 Tangri, R. and Mwenda, A.M. (2003), "Military corruption and Ugandan politics since the late
48 1990s", *Review of African Political Economy*, Vol. 30 No. 98, 539-552.
49
50

51
52 Thoumi, F. E. (2002), "Illegal drugs in Colombia: From illegal economic boom to social crisis",
53 *The Annals of the American Academy of Political and Social Science*, Vol. 582 No. 1, 102-116.
54
55
56
57
58
59
60

Transparency-International. (2019). *Corruption Perceptions Index 2018*.

Vaithilingham, S. and Nair, M. (2007), "Factors affecting money laundering: lessons for developing countries", *Journal of Money Laundering Control*, Vol. 10 No. 3, 352-366.